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No. 87-1160

In The Supreme Court of the United States

OCTOBER TERM, 1987

DUQUESNE LIGHT COMPANY
AND
PENNSYLVANIA POWER COMPANY
Appellants,

v.

DAVID M. BARASCH,
CONSUMER ADVOCATE, et al.
Appellees.

On Appeal from the Supreme Court of Pennsylvania

APPELLANTS' BRIEF IN OPPOSITION TO MOTION TO DISMISS OR AFFIRM

ALAN L. REED
WILLIAM E. ZEITER*
JOHN F. STILLMUN, III

MORGAN, LEWIS & BOCKIUS
2000 One Logan Square
Philadelphia, PA 19103
(215) 963-5367

CHRISTINE A. HANSEN
RICHARD S. CHRISTNER
LARRY R. CRAYNE
DUQUESNE LIGHT COMPANY
1 Oxford Centre
301 Grant Street
Pittsburgh, PA 15279

JAMES R. EDGERLY
STEPHEN L. FELD
PENNSYLVANIA POWER COMPANY
1 East Washington Street
New Castle, PA 16103-0891

Attorneys for Duquesne Light Company and Pennsylvania Power Company

February 17, 1988

*Counsel of Record

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The principal arguments advanced by Appellee David M. Barasch ("the Consumer Advocate") in support of his Motion to Dismiss or Affirm serve only to confirm that state-level understanding of this Court's Fifth and Fourteenth Amendment jurisprudence has drifted far wide of the mark during the decades since this Court last gave plenary consideration to a state rate order, and that there is a compelling need for guidance from this Court.

First, the Consumer Advocate accuses Appellants of seeking "to return to an era of judicial review where the minutiae of each rate decision were separately judged for their constitutional validity." (Motion to Dismiss or Affirm, p. 15.) This statement is remarkable in light of the Consumer Advocate's own reliance on the "used and useful" test and an "unbroken series of Supreme

Court decisions" (Motion, pp. 21-22) from the era predating this Court's seminal decision in *FPC v. Hope Natural Gas Co.*, 320 U.S. 591 (1944).[1] The "used and

[1]In a futile attempt at presenting three examples of post-*Hope* authority, the Consumer Advocate cites cases that are simply irrelevant to this appeal. *Market Street Railway Co. v. Railroad Commission*, 324 U.S. 548 (1945), for example, is inapposite because it involved a utility that was unable to attract enough customers to permit it to generate revenues sufficient to cover its expenses. As a result, the alleged insufficiency of the rate order resulted from market forces rather than a regulatory decision, and hence was not a taking by a state. In contrast, both Appellants could recover from their customers the amortization at issue in this case if it were allowed to be included in rates. Their inability to recover such expense is thus the result of state action, and not market forces.

Pennsylvania Electric Co. v. Pennsylvania Public Utility Comm'n, 509 Pa. 324, 502 A.2d 130 (1985) *appeal dismissed*, 476 U.S. 1137 (1986), is distinguishable on its facts. Unlike Appellants, the utilities in *Pennsylvania Electric* sought to employ *Hope* as a guarantee of a utility's financial viability. The balance of investor and consumer interest is obviously different where a facility is destroyed as a result of the "most serious [operational failure] in the history of nuclear power generating facilities in the United States," as in *Pennsylvania Electric*, 509 Pa. at 326, 502 A.2d at 131, than it is where, as in this appeal, a plant for which pre-construction expenses were incurred at the instigation of the state regulatory agency and in response to state statutory requirements for service reliability is prudently cancelled in the face of unforeseeable changes in demand for electricity.

Natural Gas Pipeline Co. v. FERC, 765 F.2d 1155 (D.C. Cir. 1985) *cert. denied* 474 U.S. 1056 (1986) applied the used and useful standard as a ratemaking principle, but, unlike the Pennsylvania Supreme Court in this case, also examined the balance between investor and consumer interests. The Court in *Natural Gas* also expressly distinguished the denial of a recovery of investment in unsuccessful experimental gas generation facilities in that case from cases permitting recovery of investment in cancelled electric generating plants. 765 F.2d at 1166-67.

Finally, the Consumer Advocate's quotation of the concurring opinion in a pre-*Hope* case, *FPC v. Natural Gas Pipeline Co.*, 315 U.S. 575, 607 (1942) requires amplification. The quoted sentence as it appears in the Consumer Advocate's Motion (Motion, p. 28) implies that the only constitutionally protected investor interests are those consistent with successful operations and the attraction of sufficient capital. That sentence, however, refers only to commission treatment of capital charges, i.e., a return *on* the shareholder's investment. Earlier on the same page, the concurring justices had stated that "[t]he investor interest is adequately served if the utility is allowed to earn the cost of service," and made clear that the cost of service included expenses. *Id.* Appellants have never sought to capitalize their investment in the four CAPCO units, but instead have sought only a recovery *of* their costs incurred in connection with such units as an amortization expense.

useful" test was at the time of *Hope* only one of several ratemaking principles that were employed as part of the constitutionally mandated "fair value" methodology required by the now-obsolete *Smyth v. Ames*, 169 U.S. 466 (1898) line of cases. The Consumer Advocate, like the Supreme Court of Pennsylvania in its decision below, seeks in this case to elevate the "used and useful" principle to a limitation of constitutional dimension on the recovery of utility investment that overrides the balancing of investor and consumer interests required by *Hope* and *Permian Basin Area Rate Cases*, 390 U.S. 747 (1968).[2]

The Consumer Advocate regards *Hope* as representing merely a doctrine of judicial restraint. In the view of the Consumer Advocate, there can be no cognizable Fifth or Fourteenth Amendment claim unless the impact of a state rate order is to bring the regulated utility to the brink of bankruptcy. The Consumer Advocate cites no reason, for there is none, why in the public utility field—as opposed to any other area of state economic regulation—a litigant should be required to demonstrate virtual economic destruction as a prerequisite to standing

[2]The Consumer Advocate's limitation of his discussion of *Permian*, this Court's most recent Fifth Amendment ratemaking decision, to the quotation of one sentence (Motion, p. 33-34), makes clear that neither the Consumer Advocate nor the Pennsylvania Supreme Court recognize that *Permian* stated a two-part standard: *If* the balancing procedure of *Permian* is followed faithfully by the ratemaking agency, 390 U.S. at 792, *then* "any rate selected from the broad zone of reasonableness" meets Fifth Amendment requirements, 390 U.S. at 770. The essence of this appeal is that the judgment below frustrated the PUC's attempt to adhere to the broadly inclusive *procedural* requirements of *Permian*, 390 U.S. at 792. These procedural requirements were recognized by the *Permian* Court to be essential as a matter of fairness in view of the relatively unstructured nature of the substantive standards of *Hope*.

to advance federal constitutional claims. Certainly *Permian* does not stand for that proposition.

The record in this case establishes an investor expectation for recovery *of* at least some part of the prudent investment undertaken at the instigation of state authorities and in response to statutory requirements for the provision of adequate electric energy supplies. The record also demonstrates the unfairness and irrationality of the effects of Act 335 and other Pennsylvania ratemaking legislation. Yet, in the face of that record, the Consumer Advocate feels free to make the broad assertion that a solvent utility can obtain no relief in this Court from the effects of a state ratemaking statute, no matter how unfair or irrational that statute may be.

As *Permian* makes clear, the "end result" aspect of *Hope* neither eliminates judicial review nor represents a bright-line guarantee of a utility's financial viability. Rather, the "end result" sought to be achieved is a utility rate order that reflects a balancing of investor and consumer interests, regardless of the numerical level of the utility's allowed rate of return. The PUC understood this teaching and struck a balance in this case. In justifying its interpretation of a statute that reduced Appellants' rates below the level of the balance struck by the PUC, the Supreme Court of Pennsylvania did not examine the balance of investor and consumer interests, but instead retrieved a ratemaking methodology from this Court's pre-*Hope* jurisprudence and invested that methodology with a contemporary constitutional dimension. Reversing that anachronistic approach would not set this Court on a course of reviewing the

"minutiae" of every state rate order, but rather would serve to instruct state ratemakers, legislators and courts not to ignore, and instead to be faithful to, the balancing of interests mandated by *Hope* and *Permian*.

The Consumer Advocate also argues (Motion, pp. 42-54) that a state legislature in enacting state ratemaking legislation is entirely unrestrained by this Court's Fifth and Fourteenth Amendment jurisprudence. So long as the Johnson Act, 28 U.S.C. § 1342, is given effect and this Court declines to review state rate orders, that may well be the rule in practice. On principle, however, it is just as impossible to reconcile with the Supremacy Clause a state's interference with a public utility's Fifth Amendment rights as it is to justify any other state attempts to restrict federally-created rights.

Given that many state legislatures seek to have their state ratemaking agency set rates at the lowest level consistent with the Fifth Amendment, there is much to be said for the Consumer Advocate's assertion (attributed to Appellants) that a state could legislate an effective ratemaking rule based on a one sentence "just and reasonable" standard. Pennsylvania, in fact, adhered to such a rule from 1937 until the Arab Oil Embargo. In any other area of Fifth Amendment practice it would be unthinkable for a litigant seriously to advance the proposition that a state legislature may denigrate from the applicable federal constitutional standard, e.g., by mandating a 10% deduction from the value of a Fifth Amendment compensation award to a condemnee for property condemned between January 22, 1980 and October 10, 1985, or by excluding constitutionally required valuation evidence. *See Monongahela*

Navigation Co. v. United States, 148 U.S. 312, 327 (1893).[3] Yet, those examples reflect the operative effect that Act 335 and other Pennsylvania ratemaking legislation, as those statutes have been construed and applied by the Supreme Court of Pennsylvania, would have on Appellants.

Reduced to its essence, the Consumer Advocate's position is one of judicial practicality. In light of the Johnson Act, which burdens this Court with the exclusive task of vindicating the Fifth Amendment rights of public utilities in a federal forum, it is said to be impractical for the federal judicial system to enforce such rights. From that proposition, it is an easy transition to the erroneous conclusion that there are no rights to enforce. With respect, Appellants believe that such a position demeans both this Court's traditional status as the ultimate guardian of federal constitutional rights and this Court's capacity to deploy effectively its limited judicial resources.

[3]In *Monongahela*, this Court held that Congress could not statutorily preclude the courts from considering the value of a company's franchise to collect tolls in determining the amount to be paid as compensation for the government's condemnation of a lock and dam belonging to the company. This Court stated:

> By this legislation congress seems to have assumed the right to determine what shall be the measure of compensation. But this is a judicial, and not a legislative, question. The legislature may determine what private property is needed for public purposes; that is a question of a political and legislative character. But when the taking has been ordered, then the question of compensation is judicial. It does not rest with the public, taking the property, through congress or the legislature, its representative, to say what compensation shall be paid, or even what shall be the rule of compensation. The constitution has declared that just compensation shall be paid, and the ascertainment of that is a judicial inquiry.

148 U.S. at 327. In contrast to the historic cases cited by the Consumer Advocate, *Monongahela*, although nearly a century old, remains a vital part of this Court's current Fifth Amendment jurisprudence. *See e.g. First English Evangelical Lutheran Church of Glendale v. County of Los Angeles*, 107 S.Ct. 2378, 2385 (1987); *Blanchette v. Connecticut General Ins. Corp.*, 419 U.S. 102, 150 n. 39 (1974).

A wide range of feasible actions are available to this Court that would both serve to remind state ratemakers, legislators and courts that utility investors continue to enjoy the protections of the Fifth and Fourteenth Amendments, and avoid re-establishing this Court as a routine participant in state ratemaking decisions. One such action, which would accomplish both objectives, would be a reversal of the judgment below on the ground that Act 335 and related Pennsylvania ratemaking legislation are inconsistent with the requirement of *Permian* that "each of the pertinent factors" be balanced in setting rates.

CONCLUSION

The Court should note probable jurisdiction and reverse the judgment below.

Respectfully submitted,

ALAN L. REED
WILLIAM E. ZEITER*
JOHN F. STILLMUN, III

MORGAN, LEWIS & BOCKIUS
2000 One Logan Square
Philadelphia, PA 19103
(215) 963-5367

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RICHARD S. CHRISTNER
LARRY R. CRAYNE
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1 Oxford Centre
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